

BEFORE THE STATE OF VERMONT
PUBLIC SERVICE BOARD

Docket No. 6120

Tariff filing of Central Vermont Public Service)
Corporation requesting a 12.9% rate increase, to)
take effect July 27, 1998)

Docket No. 6460

Tariff filing of Central Vermont Public Service)
Corporation requesting a 7.6% rate increase, to)
take effect December 24, 2000)

SURREBUTTAL TESTIMONY OF
HELMUTH W. SCHULTZ, III
AND
DONNA DERONNE

ON BEHALF OF THE
VERMONT DEPARTMENT OF PUBLIC SERVICE

April 20, 2001

Summary: In Surrebuttal Testimony, Mr. Schultz and Ms. DeRonne provide testimony and exhibits regarding the Company's overall revenue requirement, as revised. Schultz/DeRonne address the rebuttal testimonies of various CVPS witnesses with respect to payroll expense, payroll taxes, 401K expense, regulatory commission expense, Y2K cost amortization, Accounting Order amortization, utility plant in service and working capital. Schultz/DeRonne also address Mr. McKnight's rebuttal testimony with regards to the accounting implications resulting from the Department's recommendations.

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I. INTRODUCTION

Q. PLEASE STATE YOUR NAME.

A. Our names are Helmuth W. Schultz, III and Donna DeRonne.

Q. ARE YOU THE SAME HELMUTH W. SCHULTZ, III AND DONNA DERONNE THAT PREVIOUSLY FILED DIRECT TESTIMONY ON BEHALF OF THE VERMONT DEPARTMENT OF PUBLIC SERVICE IN THIS PROCEEDING?

A. Yes, we are.

Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?

A. The purpose of our surrebuttal testimony is to comment upon and rebut certain positions contained in the rebuttal testimonies of several Central Vermont Public Service Corporation (CVPS) witnesses. Failure to address certain issues contained in CVPS's rebuttal testimonies should not be taken to mean that we are in agreement with CVPS's rebuttal position. Rather, silence on issues contained with CVPS's rebuttal testimony signifies that our position remains unchanged and that our original prefiled testimony provides adequate support for our position.

Q. WHAT SPECIFIC ISSUES WILL YOU BE ADDRESSING?

A. Our surrebuttal testimony first addresses a few corrections made to the model used in determining the Department's recommended cost of service, along with the Department's overall recommended revenue requirement. Next, we address CVPS's rebuttal testimony with regards to the following specific issues: payroll and incentive compensation, 401K expense, payroll taxes, regulatory commission expense, Y2K deferrals, accounting order deferrals and amortizations, plant in service and working

capital. Finally, we address Mr. McKnight's rebuttal testimony with regards to Generally Accepted Accounting Principles and the accounting impacts of the Department's recommendations on Hydro Quebec issues.

II. OVERALL FINANCIAL SUMMARY

Q. HAVE YOU PREPARED A REVISED EXHIBIT IN SUPPORT OF THE DEPARTMENT'S REVENUE REQUIREMENT RECOMMENDATION?

A. Yes, we have prepared Exhibit DPS-L&A-5, which consists of 23 schedules. For convenience, Exhibit DPS-L&A-5 should replace Exhibit DPS-L&A-3, filed with our original testimony, in its entirety. Throughout this testimony, when a schedule is referred to, it is included in Exhibit DPS-L&A-5, unless otherwise noted. The exhibit provides a complete set of schedules. At the top right hand corner of each schedule, we indicate if it is unchanged from our previous filing, revised or a new schedule.

Q. PLEASE DISCUSS EXHIBIT DPS-L&A-5, SCHEDULE 1, WHICH IS ENTITLED "COST OF SERVICE."

A. Schedule 1 presents the overall revenue requirement, giving the effect to all the adjustments the Department witnesses, along with ourselves, are recommending. It replaces Schedule 1 from Exhibit DPS-L&A-3. This schedule includes the impact of corrections of a few errors contained in our original cost of service model, and reflects a few revisions to the Department's positions based on a review of the Company's rebuttal testimonies. As summarized on Schedule 1, the Department's analysis shows that, absent any disallowance for prudence or used and useful issues related to power supply management or the Hydro Quebec Contract, CVPS should receive a preliminary rate increase of 2.34%, or \$5,841,000. Schedule 22 reflects the effect on the cost of service of

1 a \$25,000,000 write-down as recommended in the testimony of DPS witness William
2 Steinhurst. Schedule 23 reflect the effect on the cost of service of the \$13,000,000
3 alternative write down as described in the testimony of Dr. Steinhurst.

4 Q. WOULD YOU PLEASE DISCUSS THE CORRECTIONS THAT ARE BEING MADE
5 TO YOUR ORIGINAL COST OF SERVICE MODEL?

6 A. Yes. CVPS Witness Mr. Frankiewicz pointed out a few errors in our cost of
7 service model in his rebuttal testimony. In our original calculations, we inadvertently did
8 not reflect the impact on costs allocated to wholesale sales and uncollectible expense
9 resulting from the Department's recommended adjustments. Additionally, the impact on
10 accumulated deferred income taxes resulting from several of our rate base adjustments
11 were not reflected.

12 The impact of the Department's recommended adjustments on costs allocated to
13 wholesale sales are now reflected on Schedule 1, line 22, column (F). In calculating the
14 impact, we applied the percentage of costs allocated to wholesale sales of 4.73%, which is
15 taken from the Company's original filing, to the Department's recommended reduction to
16 allocable cost of service.

17 The impact of the Department's recommendations on rate year uncollectible
18 expense is presented on Schedule 19. The calculation utilizes the same methodology and
19 uncollectible rate employed by the Company in its rate year uncollectible expense
20 calculation.

21 On Schedule 20, we calculate the impact on accumulated deferred income taxes
22 resulting from the Department's recommended adjustments to Conservation and Load
23 Management, Accounts Correcting for Efficiency, Y2K Deferred Costs, Hydro Quebec
24 Ice Storm Arbitration Deferrals and other accounting order deferrals.

1 Q. WHAT OTHER REVISIONS ARE BEING MADE TO THE DEPARTMENT'S
2 RECOMMENDATIONS?

3 A. Based on a review of the Company's rebuttal testimonies, we are making the
4 following revisions to our original recommendations: (1) payroll expense should be
5 increased from our original recommendation; (2) CVPS's requested 401K expense should
6 be reduced by \$52,000; (2) plant in service should be increased, with related revisions to
7 depreciation expense, accumulated depreciation and ADIT; (3) additional cost savings of
8 \$15,507 associated with changes to plant in service have been reflected; and (4) cash
9 working capital should be revised to reflect the impact of our other revisions. Each of
10 these modifications are discussed in further detail later in this testimony.

11 Additionally, several other Department witnesses are making revisions to their
12 recommendations, impacting the revenue requirement calculations. The revenue
13 requirement impact of those revisions, which are discussed in each witnesses respective
14 surrebuttal testimonies, are included in Exhibit-DPS-L&A-5.

15 **III. SPECIFIC ISSUES**

16 Additional Cost Savings

17 Q. WHAT ADDITIONAL COST SAVINGS ARE YOUR RECOMMENDING:

18 A. In addition to the \$20,000 described in our original testimony, the Company has
19 identified \$15,507 of cost savings associated with communication plant additions. As will
20 be discussed later in our testimony, we have added the Fiber Loop Completion project
21 work order 6246 and the Microwave Additions - 900 mhz project to our recommended
22 level of communication plant additions. Mr. Monder identified in rebuttal testimony and
23 Exhibit 5 that "An annual expense savings of \$8,307 will be realized" as a result of the 900
24 mhz Microwave Additions and \$7,200 of rate year savings will be "generated by the Fiber
25 Loop Project." As a result of the additional savings being quantified our O&M expense

1 savings correction is revised from \$20,000 to \$35,507.

2 Payroll Expense

3 Q. DID YOU REVIEW COMPANY WITNESS JOAN GAMBLE'S REBUTTAL
4 TESTIMONY REGARDING PAYROLL?

5 A. Yes. Ms. Gamble's rebuttal testimony begins with a detailed explanation of how,
6 over the last seven years, CVPS has downsized and reduced payroll and its associated
7 costs significantly. Ms. Gamble attributes this downsizing to the 1994 Company
8 restructuring, the 1997 workforce reduction and attrition. The rebuttal testimony of Ms.
9 Gamble continues with an explanation of the 1997 transformation and discusses the
10 importance of employee involvement. That discussion is followed by the identification of
11 corporate objectives, and a discussion of how the Company has developed a "win-win"
12 relationship with the union. Ms. Gamble's rebuttal testimony then addresses the
13 Company's objection to our recommended adjustments to payroll.

14 Q. PLEASE SUMMARIZE MS. GAMBLE'S TESTIMONY REGARDING INCENTIVE
15 COMPENSATION?

16 A. Company witness Gamble describes the history of the Company's incentive plan
17 and how the Company believes the plan has evolved into a balanced plan. The explanation
18 continues with an assertion that the "Company continues to raise the bar on the level of
19 performance." She then indicates that our testimony is misleading because we stated the
20 Company is charging 100% of the incentive compensation to ratepayers. Ms. Gamble also
21 claims the incentive plan encourages higher performance and productivity, and is needed
22 to be competitive with other utilities.

23 The Company witness contends that the performance compensation has, in
24 essence, eliminated the expectation for annual cost of living increases. The Company then

1 states that a portion of the total compensation “is at risk” every year based on
2 performance objectives, which is a common explanation offered by utilities. Next, a claim
3 is made that the increases in the payout percentage are known and measurable because the
4 5.6% payout in 2001 was in excess of the target payout of 4%. The Company also asserts
5 that the EIP payout for 2000, of \$932,020, validates the rate year amounts.

6 Finally, Ms. Gamble claims the Board Order in Docket No. 5701/5124 is “out of
7 date” and did not consider the non-officer incentive compensation plan at CVPS. She
8 continues by stating that all benefits from the incentive plan flow directly to the ratepayer
9 at the time of a rate case, and the “Company has designed its incentive compensation plan
10 and the overall compensation package for employees assuming a target level of payout on
11 average for employees.” (Emphasis added)

12 Q. DOES THE COMPANY’S PLAN CONTINUE TO RAISE THE BAR AS THE
13 COMPANY SUGGESTS?

14 A. The Company has not provided sufficient evidence to conclude that it has raised
15 the bar. The Company does have a relatively new comprehensive plan with many different
16 performance measures, including discretionary measures. However, the plan performance
17 measures are not raised as they should be, and in some cases measures were changed
18 before the plan had a chance to prove itself.

19 Q. HOW ARE THE PERFORMANCE MEASURES CHANGED BEFORE THE PLAN
20 HAD A CHANCE TO PROVE ITSELF?

21 A. In reviewing Gamble Exhibit 11 (the 2000 Plan) and Gamble Exhibit 12 (the 2001
22 Plan), changes were noted in the measurements identified. For example, the CORPCO
23 Strategic Business Units (SBU) financial measure, in 2000, was based on cash flow, and in
24 2001 the measure is consolidated O&M/Capital/Deferred Actual -vs- Budget. In 2000,

1 the actual customer satisfaction measurement for customer transactions was based on
2 completely satisfied responses, and in 2001, it was changed to include completely satisfied
3 and somewhat satisfied responses. (DPS 15-19(a)) The Company claims that the inclusion
4 of both categories provides a better picture of how it is doing. In 2001, the DISCO SBU
5 added five new customer satisfaction survey questions. The survey questions used in 2001
6 were changed from those used in 2000, so the Company could compare its data to the rest
7 of the industry on a routine basis. (DPS 15-19(d))

8 Q. COULD THE CHANGES BE FOR THE BETTER?

9 A. That cannot be determined. If you change the factors and determinants each year,
10 it makes it difficult, if not impossible, to measure the improvement. The incentive plan is
11 suppose to result in improvements in operations. It is difficult to measure improvements if
12 you do not have historical data for comparisons. For some measures used in the 2001
13 plan, this is the case.

14 Q. WHAT DISCRETIONARY MEASURES ARE THERE?

15 A. The 2000 plan called for "subjective assessment" by "RHY" or "Frank,"
16 "performance as judged by Frank" and "Bob Young Discretion." In other words,
17 someone will make a decision as to what percent of target an SBU achieved. For 2000,
18 some payment was made for all discretionary measurements. For the 2001 plan year,
19 approximately 39% of the measurement is discretionary.

20 Q. WHY DO YOU FEEL THE MEASURES ARE NOT RAISED AS THEY SHOULD
21 BE?

22 A. The Company indicates that the incentive compensation plan is designed to incent
23 employees to achieve performance breakthroughs, which is exactly as it should be.

1 Incentive is that which stimulates action. The Company believes that even though the
2 breakthrough was achieved, maintaining that level of accomplishment is worthy of
3 continuous incentive payment. A prime example is the 2001 plan for CORPCO SBU's
4 overall customer satisfaction. The threshold is set at 71%, the target at 78%. The 1999
5 survey results were 71.2%, the 2000 survey results were 78%. The incentive to achieve a
6 breakthrough in performance is the 82% maximum. If the Company maintains its past
7 performance, the employees are assured incentive compensation. In fact, performance
8 could drop and incentive compensation will be paid. The question must be asked, "Where
9 is the risk?"

10 The transactional survey measure, in 2001, was changed from the type of
11 satisfaction measurement used in 2000. In 1998, the combined "totally satisfied" and
12 "completely satisfied" measurement was 84.6%. In 1999, it increased to 86% and in
13 2000, it decreased to 82%. Incentive compensation will be paid if the Company attains an
14 80% combined response. This incentive pay is geared more toward "business as usual" as
15 opposed to a plan that stimulates action to achieve performance breakthroughs.

16 Q. ARE THERE OTHER MEASUREMENTS IN WHICH THE GOAL WAS NOT
17 RAISED?

18 A. Yes. The budget to actual comparison. This measurement has an extra twist to it
19 though. The 2000 budget to actual comparison shows outstanding performance for the
20 respective SBUs. It shows a positive variance of 0.3% for one SBU, while the other
21 SBUs have favorable variances (i.e., under budget) of (2.1%) to (2.4%). Yet with this
22 outstanding performance, the threshold measurement is set at 3% over budget and the
23 target at budget.

1 Q. WHAT IS THE EXTRA TWIST YOU REFERRED TO?

2 A. The 2000 budget. Performance in 1998 and 1999 was mixed, with some SBUs
3 over and some under budget. The budget for 1999 was less than the 1998 budget, and
4 actual costs in 1999 were less than 1998. However, the 2000 budget was set 10.5%
5 higher than the 1999 budget, and 6.8% higher than the 1999 actual costs. The 2000
6 budget is not consistent with the past two years budgets and is not reflective of a
7 Company in financial need. One would expect budget cuts, not increases of 6.8%, when a
8 company is in need of a rate increase. The financial performance of all the SBUs that
9 measured performance in 2000 based on budget to actual is misleading.

10 Q. IS YOUR PREFILED TESTIMONY MISLEADING WHEN YOU STATE 100% OF
11 THE INCENTIVE COMPENSATION IS BEING CHARGED TO RATEPAYERS AS
12 THE COMPANY CONTENDS?

13 A. No. The Company is including an estimated target level of incentive
14 compensation. The Company claims it is only 50% of the potential payout, and therefore,
15 they are asking that only 50% be included in rates. The truth is that it is 50% of the
16 potential payout. There are a number of problems with the Company's position. First, the
17 incentive compensation is supposed to be at risk. According to the response to DPS 3-82,
18 none of the compensation payout is guaranteed. However, the response to DPS 15-15
19 suggests otherwise when the Company claims that it "...will on average perform in 2001
20 and beyond above the threshold level of performance," and that the "expected level of
21 performance on average is the target level of performance."

22 Ms. Gamble states on page 17 of her rebuttal testimony that:

23 By having a continuous payout curve starting at the level of threshold performance
24 through the maximum level of performance, the Company has created a wide
25 "incentive zone" which maximizes the likelihood that year-to-date performance at
26 any point in the year will still be between the threshold and maximum, thus

1 providing employees an incentive for further improvement.

2 On page 25 of her rebuttal testimony, Ms. Gamble adds that the Company is asking the
3 ratepayers to pay for the target level of payout because the “levels are known and
4 realistically achievable” and “the payout has a high probability of being paid.” Finally, on
5 page 27 of her rebuttal testimony, Ms. Gamble states that despite low performance, it is
6 unlikely that no payout will be made “since our plan is designed with a large incentive
7 zone, with relatively small chance of employees receiving no payment.” This pay is not at
8 risk if that is the case. It would seem, based on Company testimony, this is a guaranteed
9 bonus under the guise of an incentive compensation plan that the Company wants
10 ratepayers to pay for 100%.

11 Q. WHAT ABOUT THE COMPANY’S CLAIM THAT THE BOARD ORDER IN
12 DOCKET NO. 5701/5124 IS OUT OF DATE?

13 A. The Company indicates that the order is 6½ years old and did not take into
14 consideration a non-officer incentive plan. In Docket No. 5983, the Board disallowed
15 100% of the non-officer incentive plan and the Management Incentive Plan. This
16 disallowance, in 1998, was based on a failure to establish true incentives, as is true in this
17 case.

18 Q. WHAT ABOUT THE BENEFITS THE COMPANY CLAIMS FLOW DIRECTLY TO
19 RATEPAYERS?

20 A. We asked the Company, in DPS 15-24, to identify specific cost savings directly
21 resulting from the 1998-2000 incentive plan achievements. The Company’s response was
22 that, “Any cost savings due to our performance oriented culture and incentive plans are
23 reflected through costs that are lower than they would otherwise have been in the rate

1 filing.” This bald assertion is not enough to demonstrate actual cost savings.

2 Q. HAVE YOU CHANGED YOUR RECOMMENDATION ON INCENTIVE
3 COMPENSATION?

4 A. Absolutely not. To allow a pro forma incentive compensation level based on a
5 plan that is not tried and true would be an unfair burden on ratepayers. The Company has
6 not demonstrated that its goals have been raised to a level that would serve as an incentive
7 to employees to excel, no cost savings have been quantified, and precedent does exist for
8 excluding costs associated with both the non-officer and the officers incentive plan. In
9 addition, the Company has not provided any rebuttal testimony regarding why a 60%
10 increase in incentive compensation is warranted when the Company claims its current
11 financial position requires it to seek an increase in rates. The Board may wish to consider
12 whether our recommended allowance of 50% of the test year incentive compensation (as
13 adjusted for wage increases) is overly generous in light of the Company’s financial
14 condition.

15 Q. WHAT OTHER PAYROLL ISSUES DID THE COMPANY ADDRESS IN ITS
16 REBUTTAL TESTIMONIES?

17 A. Company witness Gamble took exception to our adjustment to the annual pay
18 increases in the interim and rate year, the employee adjustments, the overtime adjustment
19 and an adjustment to bonuses.

20 Q. WHAT IS THE COMPANY’S OBJECTION TO YOUR ANNUAL PAY INCREASE
21 ADJUSTMENT?

22 A. The Company believes that the position by the Board in Docket No. 5372 does not
23 apply in this proceeding. It further believes, Docket No. 5546 “Clearly disposed of

1 limiting non-union increases to the increase negotiated by the union.” We disagree.
2 Docket Nos. 5428 and 5532 addressed differences in compensation levels when financial
3 factors are involved. The Company is contending that it is in need of a rate increase due
4 to its weakened financial condition. As Ms. Gamble stated in her rebuttal testimony,
5 “Much has changed in the design of incentive compensation plans.” These changes were
6 not part of Docket No. 5546. The changes have expanded the number of participants and
7 the amount of the payout.

8 Q. COULD YOU PROVIDE AN EXAMPLE OF WHY THE DISTINCTION SHOULD BE
9 CONSIDERED?

10 A. Yes. Pay increases in 1999 and 2000 were as follows:

	<u>1999</u>	<u>2000</u>
Union	2.6%	2.6%
Exempt/Office & Clerical	3.2%	6.0%
Officer	7.0%	5.1%

15 In addition, there was incentive pay that was paid in the following years for the
16 current year performance:

	<u>1999</u>	<u>2000</u>
Union	----	----
Exempt/Office & Clerical	3.4% to 7.2%	5.6% to 11.7%
Officer	16.4%	*
* To be determined		

22 If the Board limits the level of incentive compensation expense, a portion of our
23 concern is alleviated, but not all.

1 Also, the limitation of the increase is only temporary. The next time an increase in rates is
2 requested the previous wage increases are already embedded in the employee wages. For
3 example, beginning wages include the 7% increase in 1999 and the 5.1% increase in 2000
4 for officers, even when the last rate filing projected a 4% annual increase. The increase
5 that was perceived as reasonable in the last filing was exceeded and that excess is
6 automatically passed on to ratepayers.

7 Q. WHAT ABOUT THE COMPANY'S POSITION THAT LIMITING THE PAY
8 INCREASES HAMPERS THE COMPANY'S ABILITY TO PROVIDE
9 COMPETITIVE SALARIES?

10 A. Salary competition is a valid argument. However, management must be able to
11 control costs if it wants to improve its financial position. To assume that wage increases
12 are automatic because other utilities grant them is not fair to the ratepayers. The
13 Company, in Docket No. 6120, told the Board to expect an increase of 4%, then it
14 followed up with the 7.1% and 5.1% increases. These increases, above the perceived
15 reasonable increases, are permanently embedded in wages. Therefore, it is important that
16 the current increases be limited to temporarily minimize the burden automatic pay
17 increases put on ratepayers.

18 Q. IS THAT ALL THE CONCERNS WITH SALARY INCREASES?

19 A. No. The Company questions our rejecting "for no stated reason" the union
20 increase proposed for January 1, 2002. Company witness Gamble then references the
21 Department's acceptance, for rate year purposes, of the expected negotiated outcome in
22 previous rate cases. This questioning, by the Company, is wrong and without merit. The
23 rates used for union employees for period 2 and period 3 (the rate year projection), in our
24 original testimony, in Exhibit DPS L&A-3 are identical to those on Company Schedule

1 C6-1. Consequently, we allowed the union increase proposed by the Company.
2 However, since the Company has raised the issue, some concern does exist as to whether
3 the proposed increase should be included in the filing. In Docket No. 6120, as referenced
4 by the Company, the Department accepted a proposed rate that was not known and
5 measurable and was, in fact, in excess of the rate actually negotiated.

6 Q. WHY DID THE COMPANY QUESTION YOUR EMPLOYEE ADJUSTMENT?

7 A. The Company claims that utilizing the end of the test year employee level is
8 inappropriate because it is a snapshot in time and ignores the month to month fluctuations
9 that occur in employee levels. In addition, the Company feels that adjusting the end of the
10 test year employee count to the most known and measurable employee count is not
11 appropriate because January 2001 does not reflect some temporary employees and it plans
12 to add 8 positions. We disagree with the Company. Using more current known and
13 measurable information is preferable.

14 Q. PLEASE EXPLAIN WHY?

15 A. The Company's payroll expense used the test year payroll and adjusted it for pay
16 increases over three different time periods. The first time period adjusted the test period
17 to what payroll would be as of June 30, 2000. The adjustment is an estimate. To
18 eliminate one of the three estimates, we took the June 30, 2000 employees and annualized
19 their pay. Our starting point of June 30, 2000 is more known and measurable than the
20 Company's test year total adjusted for the estimate of increases granted during the test
21 year.

1 Q. WHAT ABOUT THE COMPANY'S CLAIM THAT THE ADJUSTMENT IS NOT
2 APPROPRIATE BECAUSE JANUARY AND JUNE ARE NOT COMPARABLE DUE
3 TO TEMPORARY EMPLOYEES HIRED TO PERFORM SUMMER WORK?

4 A. June includes summer help. Based on the Company's responses to data requests,
5 the vacancies are full-time positions and the number of seasonal temporary employees has
6 been reduced. However, this issue is moot.

7 Q. WHY IS THIS ISSUE MOOT?

8 A. Based on the response to DPS 15-17, the employee compliment is now at 556;
9 therefore, our recommended employee adjustment is withdrawn with reservation.

10 Q. WHAT RESERVATIONS DO YOU HAVE ON WITHDRAWING YOUR
11 RECOMMENDATION?

12 A. Ms. Gamble's rebuttal testimony discusses, in detail, the incentive plan and how
13 the Company employees deserve the incentive compensation because of their fine
14 performance. Company testimony boasts of its accomplishments in reducing the
15 workforce and generating millions of dollars in savings. What is not discussed, in detail, is
16 that ratepayers are paying for that restructuring and workforce reduction, and an increase
17 in employees. In 2000, performance based on budget looks good, as previously discussed,
18 except exempt payroll was over budget. In fact, on average the Company was over
19 budget by eight (551 -vs- 543) employees in the year 2000. The count, as of March 2001,
20 is 556 and the Company is planning to hire more employees. Ratepayers are actually
21 paying twice, first for the downsizing and also for the replacements.

1 Q. IS THE COMPANY'S CONCERN REGARDING YOUR OVERTIME
2 CALCULATION VALID?

3 A. For consistency purposes, the percentage identified by the Company should have
4 been used. The adjustment for overtime has been corrected on Schedule 7, page 3 of 3, to
5 reflect the proper percentages. The proper level of overtime for the rate year is
6 \$2,335,611.

7 Q. ARE THE COMPANY ARGUMENTS FOR USE OF TEST YEAR OVERTIME
8 INSTEAD OF YOUR RECOMMENDED AVERAGE LEVEL VALID?

9 A. No. The test year, in this case, not only includes two major storms, it also includes
10 employees that are part of the purported workforce reduction. The test year level of
11 overtime expense of \$2,428,257 (before the Company adjustment) is higher than any of
12 the last four calendar years. The test year overtime level is not reflective of normal
13 operating conditions. The Company provided no justification as to why the excessive
14 level of overtime in the test year is appropriate.

15 Q. HAS THE BOARD ADOPTED AVERAGING IN THE PAST?

16 A. Yes. The Board has used averaging to level out unusual fluctuations from year to
17 year. Averaging has been used, in the past, to determine the pro forma level of tree
18 trimming expense, O&M payroll expense factors, regulatory commission expense,
19 uncollectibles, etc. The only valid alternative to averaging would be to use the last known
20 and measurable normal year of overtime, which would be \$1,836,632 from the calendar
21 year 2000.

1 Q. DOES THE COMPANY'S REBUTTAL TESTIMONY CHANGE YOUR
2 RECOMMENDATION ON DISCRETIONARY BONUSES?

3 A. No. The only alternative recommendation would be to remove it all. Employees
4 are compensated for the services they perform. The incentive pay, or so called "at risk"
5 pay, is in addition to the base pay. Company testimony makes it clear the pay is not really
6 at risk since it is "unlikely" that a payout will not be made. In addition, the Company has
7 discretionary bonuses that "are an important part" of the "overall compensation structure."
8 The test year included \$66,532 for storms and \$63,212 for "other bonuses related to
9 outstanding performance." The bonus payout includes signing bonuses and severance
10 payouts. The question that needs to be answered is "How many bonuses is it reasonable
11 for the ratepayer to pay?"

12 Q. DID YOU IGNORE THE DISCRETIONARY BONUS FOR 1998 AS MS. GAMBLE
13 STATES?

14 A. Yes. The 1998 bonus of \$447,878 is not comparable to the \$164,161 and
15 \$181,385 for 1999 and 2000, respectively. Besides, the bonuses in 1999 and 2000 are
16 more reflective of the Company's evolving compensation package (i.e., the incentive plan
17 in 1998 was different from 1999 and 2000). Our position remains, \$200,000 is more than
18 a reasonable level for discretionary bonuses and ratepayers should not have to pay more
19 than half. The \$100,000 included in payroll is sufficient.

20 Q. WHAT IS YOUR REVISED RECOMMENDATION FOR PAYROLL EXPENSE?

21 A. With the elimination of our employee adjustment and the revision to the overtime
22 adjustment, our calculated rate year payroll expense of \$22,817,115 is reasonable. As
23 shown on revised Schedule 7, the Company's request for \$24,446,215 is overstated by
24 \$1,629,100.

1 Payroll Tax Expense

2 Q. DOES YOUR ADJUSTMENT TO PAYROLL AFFECT YOUR PAYROLL TAX
3 EXPENSE ADJUSTMENT?

4 A. Yes. Using the Company's effective tax rate of 7.3%, Social Security taxes should
5 be reduced by \$118,924. This adjustment is 7.3% of the \$1,619,100 payroll reductions
6 discussed above.

7 Q. WHAT ABOUT COMPANY WITNESS HOLTMAN'S CLAIM THAT YOU SHOULD
8 USE THE 7.65% RATE AUTHORIZED BY LAW?

9 A. An adjustment using the 7.65% tax rate, although favorable to ratepayers, is totally
10 inappropriate. The employer contribution for Social Security is paid on a fixed base.
11 Once the employee reaches that base no more taxes are paid. Therefore, it is appropriate
12 for Social Security tax expense to be calculated based on an effective tax rate as we did.
13 The 7.3% rate was calculated by dividing the Company's \$1,774,931 Social Security tax
14 expense by the Company's \$24,446,216 requested payroll expense. The 7.3% is the
15 effective tax rate and the correct rate to use.

16 401K Expense

17 Q. IS IT TRUE THAT YOU DID NOT REFLECT THE IMPACT ON 401(K) EXPENSE
18 RESULTING FROM YOUR RECOMMENDED PAYROLL EXPENSE REDUCTION
19 AS COMPANY WITNESS FRANKIEWICZ CONTENTS IN HIS REBUTTAL
20 TESTIMONY?

21 A. Yes. Since, the Company's 401(K) is automatically adjusted based on the payroll
22 adjustment, a calculation has been made to adjust the 401(K) expense accordingly. Using
23 the Company methodology, the Company's rate year expense of \$780,433 should be
24 reduced by \$52,027 to \$728,406.

1 Regulatory Commission Expense

2 Q. IN YOUR PREFILED TESTIMONY, YOU RECOMMENDED AN ADJUSTMENT TO
3 REGULATORY COMMISSION EXPENSE. COULD YOU PLEASE SUMMARIZE
4 YOUR RECOMMENDATION?

5 A. Yes. In determining the rate year level of regulatory commission expense, the
6 Department has historically approved a normalization adjustment based on the five-year
7 average level of regulatory commission expense. Since the level of regulatory commission
8 expense fluctuates from year to year based on various factors, such as the level of
9 regulatory cases in progress, there is no way to know, with certainty, what the actual rate
10 year cost level will be. Consequently, a normalized amount is typically adopted based on a
11 five-year average cost level. In our prefiled testimony, we recommended that costs
12 associated with two specific cases be removed for purposes of calculating the five-year
13 average cost level. The cases include Vermont PSB Docket No. 6133 - Holding Company
14 and the Patch Case in Federal District Court. Removal of these two dockets results in a
15 \$278,077 reduction in CVPS's requested regulatory commission expense.

16 Q. DID THE COMPANY REBUT YOUR RECOMMENDATION?

17 A. Yes. CVPS Witness Mr. Frankiewicz addressed our recommendation in his
18 rebuttal testimony. Essentially, he disagrees with the removal of the Vermont PSB
19 Docket No. 6133 - Holding Company and the Patch Case costs from the determination of
20 the five-year average, normalized cost level.

21 Q. PLEASE DISCUSS MR. FRANKIEWICZ'S REBUTTAL TESTIMONY WITH

1 REGARDS TO THE COSTS ASSOCIATED WITH DOCKET NO. 6133.

2 A. The purpose of Docket No. 6133 was for CVPS to set up a separate holding
3 company in preparation for potential electric industry deregulation. Mr. Frankiewicz
4 indicates that he believes the associated costs are legitimate and that the use of a holding
5 company has become "...the standard for American utility companies..." While these
6 contentions may be true, it does not change the fact that the primary beneficiaries of a
7 separate holding company is the Company's shareholders, not its ratepayers. We continue
8 to recommend that the costs associated with this docket, which were \$203,498 in the 12-
9 months ended June 30, 1999, and \$187,994 during the 12-months ended June 30, 2000,
10 be removed in calculating the five-year average regulatory commission expense level.

11 Q. PLEASE DISCUSS THE PATCH CASE.

12 A. As indicated in our original testimony, the five-year average regulatory expense
13 calculation includes \$822,581 recorded as expense on CVPS's books in the 12-months
14 ended June 30, 1999 and \$146,995 in the 12-months ended June 30, 2000 for the Patch
15 Case. This is 50% of the total costs associated with the case in those periods. The
16 remaining 50% was recorded on the books of Connecticut Valley Electric Company Inc.
17 (CVEC), which is Central Vermont's wholly owned subsidiary that serves New Hampshire
18 and is regulated by the New Hampshire Public Utility Commission (NHPUC). The
19 inclusion of this New Hampshire case has a considerable impact on the five-year average
20 cost level calculation.

21 A more detailed discussion of the Patch Case is included in our prefiled testimony;
22 consequently, we will not reiterate that testimony here. However, we would like to repeat
23 that the case involves decisions made by the New Hampshire Public Utility Commission
24 (NHPUC) regarding costs incurred by CVEC to be passed on to CVEC's New Hampshire
25 customers. It involved NHPUC's determination that Connecticut Valley acted imprudent

1 by not terminating the wholesale contract between CVEC and CVPS as the rates were
2 above market price. This was not a Vermont case. A detailed description of the case,
3 which was taken from CVPS's Form 10-Q for the period ended September 30, 2000, was
4 provided in Exhibit DPS-L&A-4, pages 10 through 19, filed with our original testimony
5 on March 9, 2001. It remains our position that Vermont ratepayers should not be
6 responsible for funding any of the associated legal costs, and should definitely not be
7 responsible for 50% of those costs.

8 Q. DOES THE COMPANY DENY THAT THIS WAS A NEW HAMPSHIRE CASE
9 INVOLVING CVEC?

10 A. No, it does not. In rebuttal testimony, Mr. Frankiewicz states that "...loss of the
11 Patch Case and/or the FERC proceeding would mean the costs in question would or at
12 least could be reallocated to the Vermont retail customers of Central Vermont." Mr.
13 Frankiewicz's argument, in essence, is that the loss of the Patch Case would result in a
14 reallocation or shift of costs from a wholesale customer (CVEC) to the Vermont
15 ratepayers. The witness discusses several past instances in which wholesale customers
16 purchased less wholesale power from CVPS or discontinued purchasing wholesale power
17 and the wholesale cost allocations decreased, resulting in increases in retail allocation.

18 In the Patch Case, the Company involved is an affiliated Company, not an
19 independent party. Additionally, a significant factor causing the power costs, under the
20 contract between CVPS and CVEC, to be above market rates is the Hydro Quebec
21 contract. It is not reasonable for the Company to presume that the Vermont Public
22 Service Board would allow the above market costs for the portion of the Hydro Quebec
23 contract that was used to serve an affiliated company's New Hampshire customers to
24 become the responsibility of CVPS's Vermont retail customers. The Company's attempt
25 to do so, had CVEC been unsuccessful in the Patch Case, would be a highly contested

1 issue. Other Department witnesses in this proceeding discuss the Hydro Quebec contract
2 issues in greater detail in their testimonies. Furthermore, the Company has not presented
3 compelling reasons for allocating to CVPS, in Vermont, a full 50% of legal costs incurred
4 in a case involving a New Hampshire affiliated company and New Hampshire regulatory
5 decisions.

6 Q. BEYOND THE NATURE OF THE PATCH CASE, AND THE FACT THAT IT IS A
7 NEW HAMPSHIRE CASE INVOLVING AN AFFILIATED COMPANY, ARE THERE
8 ANY ADDITIONAL REASONS THAT THIS CASE SHOULD BE EXCLUDED IN
9 DETERMINING THE FIVE-YEAR AVERAGE?

10 A. Yes. The purpose of using a five-year average cost level for regulatory
11 commission expense is that the future cost level is not known. Consequently, a historical
12 average cost level is used to determine a normalized cost level that would be
13 representative of going-forward costs. The purpose of a normalization adjustment is not
14 to specifically allow recovery of past costs that have been incurred. Rather, the purpose is
15 to determine what a normal, on-going cost level would be. The Company has the ability
16 to request an accounting order from the Board to defer costs for future consideration.
17 The costs associated with the Patch Case were not deferred for future consideration.
18 They were recorded as a period expense on the Company's books. It is our position that
19 this one case had such a significant impact on the determination of the five-year average
20 cost level that the result is not reflective of a "normalized," on-going cost level. Costs
21 associated with 24 separate cases were recorded as regulatory commission expenses
22 during the 12 month period ended June 30, 1999, yet the Patch Case consisted of over
23 50% of the total regulatory commission expenses recorded on CVPS's books for that
24 year. The costs for that year were the highest amount included in determining the five-
25 year average expense level. This one case, which is not even a Vermont regulatory

1 commission case, greatly skewed the overall five-year average calculation.

2 Q. HOW DOES THE LEVEL OF REGULATORY COMMISSION EXPENSE
3 REQUESTED BY CVPS IN THE CURRENT CASE COMPARE TO THAT OF THE
4 PRIOR RATE CASE?

5 A. In Docket No. 6120, the Company requested a regulatory commission expense
6 level of \$691,405. This amount was based on the five-year average for the period April
7 1993 through March 1998. In the current case, the Company is requesting an expense
8 level of \$992,504. This is an increase of over \$300,000 since the last case. We continue
9 to recommend our adjustment, which reduces rate year regulatory commission expense by
10 \$278,000, be adopted by the Board.

11 Y2K Cost Amortization

12 Q. WOULD YOU PLEASE SUMMARIZE YOUR POSITION WITH REGARDS TO THE
13 Y2K COST DEFERRAL?

14 A. Yes. CVPS deferred \$30,790 of Y2K costs incurred in December 1997, \$2.173
15 million of Y2K costs incurred in 1998, \$562,141 incurred in 1999 and \$130,388 incurred
16 in 2000. These amounts resulted in a total Y2K deferral of \$2,896,321, which CVPS
17 began amortizing in January 2000. CVPS requested an annual amortization expense of
18 \$534,381 and rate base treatment for the average unamortized balance. In an accounting
19 order, the Board authorized CVPS to defer Y2K costs incurred in 1998 only, not those
20 costs incurred in 1997, 1999 and 2000. The bulk of the costs were incurred during 1998.
21 We recommended, and continue to recommend, that the Y2K amortization expense and
22 unamortized balance for inclusion in rate base be based only on the amounts specifically
23 approved for deferral by the Board in its August 31, 1998 Accounting Order.

1 Q. AT PAGE 2 OF HIS REBUTTAL TESTIMONY, JOHN HOLTMAN CONTENDS
2 THAT YOUR EXCLUSION OF THE COST INCURRED IN YEARS OTHER THAN
3 1998 IS BASED ON YOUR INTERPRETATION OF THE ACCOUNTING ORDER,
4 AND THAT HE DISAGREES WITH YOUR INTERPRETATION. COULD YOU
5 PLEASE COMMENT.

6 A. Yes. Our recommendation is not based on our “interpretation” of the accounting
7 order. Rather, it is based on the clear and specific language of the accounting order.
8 There was no need for “interpretation” as the language was clear and precise. Mr.
9 Holtman contends at page 2 of his testimony that, “The order itself is internally
10 inconsistent and therefore ambiguous.” There is no inconsistency or ambiguity in the
11 accounting order. It is clear and concise. In fact, the wording under the “Order” section
12 of the August 31, 1998 Accounting Order, items number 1 through 7, are exactly the
13 same, word for word, as the Company’s draft Accounting Order provided by CVPS to the
14 Board with its request for the Accounting Order. We find it ironic that the Company now
15 contends that this accounting order, in which the Company is the one who drafted the
16 language appearing in the ordering section, is ambiguous. The August 31, 1998
17 Accounting Order was attached to Mr. Holtman’s rebuttal testimony as CVPS Exhibit
18 Holtman - 8. The Company’s request for the Accounting Order, along with its proposed
19 draft accounting order, was attached as CVPS Exhibit Holtman - 1.

20 Q. YOU INDICATE THAT THE LANGUAGE IN THE ORDER LIMITING THE
21 DEFERRAL TO 1998 COSTS IS CLEAR AND CONCISE. COULD YOU PLEASE

1 IDENTIFY THE PART OF THE ORDER THAT SPECIFICALLY LIMITS THE
2 COSTS TO THOSE INCURRED DURING 1998?

3 A. Yes. The August 31, 1998 Accounting Order specifically states as follows, under
4 paragraph 1 of the "Order" section:

5 The Company is authorized to defer and shall defer the recognition of the Year
6 2000 compliance costs that would otherwise be recognized in 1998, and shall
7 commence the amortization of such costs on January 1, 2000. Such costs shall be
8 recorded in FERC account 182.3 and amortized over five years.
9

10 This paragraph in the Order specifically limits the amounts to "costs that would
11 otherwise be recognized in 1998..." This is identical to the language recommended by the
12 Company in its request for an accounting order. In the first paragraph of the August 31,
13 1998 Accounting Order, the Board states, "For the reasons explained below, and subject
14 to the conditions set forth below, the Board grants the requested accounting order."
15 (Emphasis added) One of the specific conditions in the order was the limitation to the
16 1998 costs. The Accounting Order, which was filed as CVPS Exhibit Holtman - 8, is not
17 "internally inconsistent" or ambiguous as purported by Mr. Holtman.

18 Q. MR. HOLTMAN ATTACHES NUMEROUS DOCUMENTS TO HIS TESTIMONY
19 WHICH HE CLAIMS DEMONSTRATE THE "TRUE INTENT" WITH RESPECT TO
20 THE ACCOUNTING ORDER. WOULD YOU PLEASE COMMENT ON HIS
21 POSITION?

22 A. Yes. While we will not go point by point through each of his attachments, we will
23 comment that there is nothing contained in any of the ten attachments that specifically
24 state that Y2K costs incurred during the periods 1997, 1999 and 2000 would be included
25 in the deferral. The Company's original request for an Accounting Order, dated March
26 10, 1998, indicated that, "The Company estimates that it will incur incremental costs of

1 approximately \$2.1 million during 1998 to achieve compliance on a timely basis.”

2 (Emphasis added) The letter also states that the “...significant one-time cost to extend the
3 useful life of existing hardware and software systems would, lacking the requested
4 Accounting Order, be prohibitively expensive and distort the Company’s income statement
5 for 1998.” (Emphasis added) At that time, the Company knew it would incur costs
6 associated with the Y2K project after 1998, and that it had incurred a small level of costs
7 in 1997 for the project, yet it did not include those years in its request. The bulk of the
8 costs (approximately \$2.2 million of the total \$2.9 million incurred) was, in fact, incurred
9 during 1998. While this \$2.2 million, incurred during 1998, could have distorted the
10 Company’s income statement for 1998, as contended by the Company in its request, the
11 remaining years would not have had as large of an impact on the income statement had the
12 costs been expensed as incurred.

13 Q. IS NOW THE APPROPRIATE TIME TO CHALLENGE THE LANGUAGE OF THE
14 1998 ACCOUNTING ORDER?

15 A. No. It is not appropriate to go back over 2½ years after the fact and challenge the
16 clear and specific language of the Order. It was the Company who essentially wrote a
17 substantial part of the language included in the August 31, 1998 Accounting Order. At
18 the very least, the Company should have carefully reviewed the language contained in the
19 Accounting Order (or any Accounting Order for that matter) when received and
20 challenged any of the specific language contained in the Order shortly after the Order date.
21 It is not appropriate to go back and try to guess each of the parties intent over 2½ years
22 after the fact.

23 Accounting Order Amortization

24 Q. MR. HOLTMAN PROVIDES UPDATES TO THE RETAIL CHOICE ACCOUNTING

1 ORDER DEFERRAL AND THE SMALL POWER PRODUCES DOCKET NO. 6270
2 DEFERRAL IN HIS REBUTTAL TESTIMONY. HAVE YOU REFLECTED HIS
3 UPDATES IN YOUR EXHIBIT?

4 A. Yes, to a degree. Consistent with our initial testimony, we recommend that the
5 incremental revenues from the deseasonalization of rates first be used to offset the actual
6 costs deferred for these two dockets. The remainder of the incremental revenues could be
7 used to offset additional future costs incurred for those two dockets, with the remainder
8 being used to offset Hydro Quebec ice storm arbitration costs. In Schedule 12, we
9 updated the calculation of the remaining incremental revenues to account for the actual
10 costs incurred for the Retail Choice Accounting Order and Small Power Produce's docket
11 through February 28, 2001. These include the actual costs incurred through that date, as
12 provided in Mr. Holtman's rebuttal testimony and CVPS Exhibit Holtman - 9. It also
13 includes corrections of the Company errors in the deferral amounts discussed in Mr.
14 Holtman's rebuttal testimony. As shown on Schedule 12, the actual costs for the two
15 dockets through February 28, 2001 results in \$3,056,399 of remaining incremental
16 revenues to be used to offset future costs for those two dockets and the Hydro Quebec ice
17 storm arbitration costs.

18 Q. DOES THIS UPDATE HAVE ANY IMPACT ON YOUR REVENUE REQUIREMENT
19 CALCULATIONS?

20 A. No, it does not. As addressed in our original testimony, we recommend that the
21 Hydro Quebec ice storm arbitration costs, after the offset for the remaining incremental
22 revenues, continue to be deferred at this time, with no rate base treatment. Consequently,
23 the update of the Accounting Order costs does not impact our revenue requirement
24 calculations.

1 Hydro Quebec Ice Storm Arbitration Costs

2 Q. MR. HOLTMAN ADDRESSES YOUR RECOMMENDATION THAT THE HYDRO
3 QUEBEC ICE STORM ARBITRATION COSTS CONTINUE TO BE DEFERRED AT
4 THIS TIME IN HIS REBUTTAL TESTIMONY. DOES HIS REBUTTAL
5 TESTIMONY CHANGE YOUR POSITION?

6 A. No, it does not. We continue to recommend that these costs be deferred until the
7 outcome of the arbitration is known and measurable. The costs associated with the
8 arbitration should be matched with the benefits resulting from that arbitration. At page 91
9 of his rebuttal testimony, when discussing the Hydro-Quebec ice storm arbitration,
10 Company witness Mr. Boyle indicates that, "The Company has always expressed a
11 willingness to pass through the net benefits of any favorable arbitration decision." The
12 costs associated with the arbitration should be matched with the benefits resulting from
13 that arbitration, when such benefits to ratepayers occur. In response to DPS 16-23, the
14 Company indicated that it expects the arbitration award to be rendered as early as April
15 17, 2001. As of the date of writing this testimony, the arbitration decision has not been
16 released although imminently expected. By the time this docket goes to hearing, more
17 information may be available.

18 Q. MR. HOLTMAN RECOMMENDS THAT IF THE HYDRO QUEBEC ARBITRATION
19 COSTS CONTINUE TO BE DEFERRED, THE COMPANY SHOULD BE
20 PERMITTED TO APPLY CARRYING COSTS TO THE BALANCE. DO YOU
21 AGREE?

22 A. No, we do not. The Company's shareholders will also benefit if the Company is
23 successful in the arbitration. As indicated in our original testimony, it is quite possible that
24 ratepayers will be required to fund the arbitration costs at some point in the future, after
25 the matter is resolved. They should not be required to also provide a return on these

costs.

Utility Plant In Service

Q. PLEASE DISCUSS THE COMPANY'S CONCERNS WITH YOUR APPLICATION OF THE KNOWN AND MEASURABLE STANDARD.

A. On page 12 of Company witness Frankiewicz' rebuttal testimony, he states the following:

Beginning on page 36, line 16, Schultz/DeRonne describe the known and measurable standard they have used in arriving at their adjustments. A fair interpretation of their testimony denies a project's being a rate base addition (1) because a project has not started, (2) because a project does not have a work order number assigned, (3) because the project costs are estimated, (4) because in their opinion there is no assurance that the estimate is reasonably accurate, or (5) because it is not known if any cost savings will result from the project.

This assessment by the Company is not accurate. Our recommendations were based on the facts presented to us in the proceeding, our application of the known and measurable standard in past proceedings and the Board's acceptance of our application of the standard in past proceedings.

Q. DID YOU DISALLOW ALL PROJECTS THAT HAVE NOT STARTED?

A. No. Blanket work orders in the rate year have not been started and we allowed all, or an adjusted level of costs, for all of the blanket work orders. Below are some projects that incurred no costs, but we did allow:

<u>Plant</u>	<u>Project</u>	<u>Period</u>
Transmission	Loadbreak Switch Jeffersonville (WO 6201)	Interim
	Reconductor N. Elm St. (WO 9945)	Rate

1	Distribution	Replace Mt. Holly X Former	Interim
2	Communications	Purchase Tower Site (WO 6232)	Interim
3		Test/Devel. IVR System	Interim
4	Info Systems	Client Server	Interim
5		QA RS/6000 Replacement	Interim
6		WMS Transmission	Rate
7	Facilities	Engineering HVAC	Interim
8		Systems Underground Tank	Interim
9		Systems Storage	Rate
10	Production	Silver Lake Penstock (WO 6261)	Rate

11 The Company appears to have been overly presumptuous in suggesting that we did
12 not allow a project because it had not been started.

13 Q. DID YOU DISALLOW A PROJECT JUST BECAUSE IT DID NOT HAVE A WORK
14 ORDER NUMBER?

15 A. No. A number of the projects listed above do not have work order numbers,
16 therefore, this allegation by the Company is also without merit.

17 Q. IS THE USE OF PROJECT ESTIMATES ALONE REASON ENOUGH FOR YOU TO
18 DISALLOW A PROJECT?

19 A. No. Costs on the projects listed above are based on estimates. The Company has
20 once again improperly characterized our testimony.

21 Q. IS IT FAIR TO SAY THAT YOU DISALLOWED A PROJECT BECAUSE THERE
22 WAS NO ASSURANCE THAT THE ESTIMATE PROVIDED WAS REASONABLY

1 ACCURATE?

2 A. No. While it is a major factor in making the final determination, it is not the sole
3 factor. The same explanation would apply to cost savings, the fifth item listed by Mr.
4 Frankiewicz. The testimony presented by the Company suggests that a single item is
5 sufficient for us to consider a project as not being known and measurable. This is not the
6 case.

7 Q. PLEASE EXPLAIN YOUR BASIS FOR DISALLOWANCE OF A PROJECT.

8 A. The known and measurable changes to the test year have to have a high probability
9 of occurring and is to be quantifiable with a reasonably high degree of accuracy. In
10 Docket No. 5983, the Board, in discussing the use of known and measurable plant
11 additions, made reference to the fact that "The Company is only entitled to a return on
12 plant that is actually serving ratepayers." This concept is very important in assessing
13 whether plant projections should be included in rate base. The assessment process is a
14 multi-step process.

15 A significant number of the projects recommended for disallowance are those
16 identified as rate year additions. In determining whether the projects have a high
17 probability of being completed in the rate year and that the cost estimate has been
18 determined with a reasonably high degree of accuracy, we considered most, if not all, the
19 items identified on pages 36-39 of our March 9, 2001 prefiled testimony.

20 Q. PLEASE PROVIDE A SCENARIO OF THE PROCESS.

21 A. The first question is, "Has a work order been issued?" The issuance of a work

1 order provides a significant amount of detail and is an indicator the project may be starting
2 soon. Emphasis on the “may” because it is not a guarantee. The work order provides a
3 cost estimate (sometime supported by quotes), a description of the project, an estimate of
4 plant retirement cost, a projected completion date, budget reference and, in some cases, a
5 cost benefit analysis.

6 The importance of this information will vary. As discussed in our prefiled
7 testimony, the actual completion date for test year and interim year projects was found to
8 be later, and in a number of instances significantly later, than the projected date on the
9 work order. Since a majority of the rate year projects do not have a work order (i.e.,
10 indicating the process is beginning), there is very limited assurance the project will be
11 underway and completed before the end of the rate year. The Company did not rebut our
12 testimony on the historical slippage.

13
14 Q. WHAT ABOUT THE COMPANY’S TESTIMONY THAT THE INTERIM AND RATE
15 YEAR ARE REASONABLE BASED ON HISTORICAL CAPITAL SPENDING?

16 A. In determining whether the projected costs are reasonable and will be incurred
17 during the rate year, the Board has generally considered the costs, except for blankets on a
18 “project by project” basis, not on total expenditures alone. Beyond that, the Company’s
19 representation of what CVPS Exhibit Frankiewicz 6 (Frankiewicz 6) shows, is misleading.
20 What needs to be considered before discussing Frankiewicz 6, is the Company’s testimony
21 regarding its weakened financial condition over the past few years. Take special note of
22 spending in 1999 and 2000.

23 Q. WHAT DIFFERENCE IS THERE IN LOOKING AT THE 1999 AND 2000 SPENDING

1 VERSUS THE AVERAGE SPENDING, THE INTERIM AND THE RATE YEAR
2 TOTALS STILL APPEAR TO BE IN LINE?

3 A. The totals appear to be, but they are not comparable. The capital spending
4 includes growth. The interim and rate year amounts purportedly do not. A line-by-line
5 analysis is more informative.

6 First, production spending projected in each of the interim and rate years is in
7 excess of \$1,000,000. Spending was \$353,000 and \$905,000 in 1999 and 2000,
8 respectively. A two-year average of \$629,000 compared to the two-year average in the
9 filing of \$1,073,000. This does not support the claim that in excess of \$1,000,000 will be
10 spent each year.

11 Next, transmission spending is estimated at \$1,865,000 and \$1,552,000 in the
12 interim year and rate year, respectively. This is approximately four times the 1999
13 spending and twice the year 2000 spending. Again, no support for the Company's claim
14 that the spending will occur.

15 Distribution substations projected spending is \$378,000 and \$875,000 in the
16 interim year and rate year, respectively. We did not disallow any of the interim year, so
17 the only issue is the rate year. With actual spending of less than \$300,000 in 1999 and
18 again in 2000, limited assurance exists for spending \$875,000 in the rate year.

19 The non-growth distribution purchases projected spending for the interim year and
20 rate year is \$1,536,000 and \$1,708,000, respectively. The approximate actual non-growth
21 spending in 1999 and 2000 is \$1,249,976 (\$2,489,000 x 50.22%) and \$1,207,791
22 (\$2,405,000 x 50.22%), respectively. Our adjustments reducing the interim year costs by
23 \$75,000 and the rate year costs by \$250,000 are considered conservative when comparing
24 the projected spending to actual.

25 The distribution lines reconstruction amounts present a dilemma.

1 Q. WHAT IS THE DILEMMA ASSOCIATED WITH THE DISTRIBUTION LINES
2 RECONSTRUCTION AMOUNTS?

3 A. The actual spending amounts on CVPS Exhibit Frankiewicz 6 (Frankiewicz 6) are
4 significantly higher than the actual amounts, by work order, provided in response to DPS
5 3-97. Since DPS 3-97 requested comparable information to each of the distribution
6 reconstruction categories presented in the Company's filing, the response is considered to
7 be the correct amounts to be used in determining the reasonableness of the projected
8 interim year and rate year spending. This information is reflected on Exhibit DPS-L&A-5,
9 Schedule 14. The sum of the four-year average of line reconstruction costs is \$2,978,063
10 (lines 7, 8 and 9). This is significantly lower than the projected interim year spending of
11 \$5,901,000 and the projected rate year spending of \$5,839,000.

12 Q. WILL THE SAME RESULTS BE FOUND IN COMPARING THE PROJECTED
13 FACILITIES ADDITIONS?

14 A. Yes. The projected spending for the interim year and rate year is \$1,061,000.
15 This is approximately 60% higher than the \$649,000 spent in 1999 and 2000.

16 Q. IS THE PROJECTED SPENDING ON INFORMATION SYSTEMS AS
17 REASONABLE AS IT APPEARS?

18 A. No. The interim year amount is misleading because it is net of \$3.3 million in
19 retirements. However, we are not recommending a disallowance of any of the interim
20 adjustments, and as this will be discussed later, we will be changing our recommendation
21 on rate year additions.

1 Q. PLEASE CONTINUE.

2 A. The last category is communication systems. It does not matter what you review
3 in this category because, in all scenarios, the interim and rate year spending is not
4 supported by historical spending.

5 Q. IS THERE MORE YOU CONSIDER WHEN DETERMINING WHETHER THE
6 PROJECT IS KNOWN AND MEASURABLE?

7 A. Yes. When a project does not have a work order number and historical spending
8 does not justify the overall spending by function or category we will assess the estimate,
9 the supporting detail for the estimate, responses to data requests and Company testimony.

10 Q. DID THE COMPANY'S REBUTTAL TESTIMONY PROVIDE ANY INDICATION
11 AS TO HOW KNOWN AND MEASURABLE THE COMPANY'S INTERIM AND
12 RATE YEAR PROJECTS ARE?

13 A. Yes. On Exhibit DPS-L&A-5, Schedule 21, we have summarized the projects
14 where differences exist. There is a column for our position, the Company as originally
15 filed, the Company rebuttal position and a column that indicates comments by the
16 Company in the rebuttal testimony, which includes in brackets the date, which is generally
17 the originally filed completion date for the project. The Company witnesses, although
18 steadfast in their position for the majority of the projects, have removed a number of
19 projects, corrected errors, changed the projected costs and completion dates and even
20 added some projects.

1 Production

2 Q. ARE THERE ANY SPECIFIC ISSUES THE COMPANY REBUTTED ON
3 PRODUCTION PLANT YOU WISH TO DISCUSS?

4 A. Yes. For the interim period, we adjusted the Rutland GT5 Fuel Control Upgrade,
5 WO 6219, upward to the actual cost of \$321,379 based on the Company response to DPS
6 4-32. The Company has now indicated that the \$321,379 should be \$268,158 because of
7 an error in estimating the year-end accrual. We agree, this project should be revised to
8 \$268,158. However, an estimating error of 20% on a job in process raises a concern as to
9 the reliability of estimates for jobs not yet started.

10 Q. ARE THERE OTHER PROJECTS FOR WHICH YOU HAVE CHANGED YOUR
11 ORIGINAL RECOMMENDATION?

12 A. No. Even though the Company insists that the majority of the projects in dispute
13 will occur at the cost in the filing, they have not provided sufficient support. The only
14 evidence provided is the Company's testimony.

15 Q. DID YOU REQUEST SUPPORT?

16 A. Yes. In DPS 4-32, we asked that for projects not started or not completed
17 provide supporting detail for the estimated costs. The responses for projects that we
18 recommended be disallowed are as follows:

19 Clark Falls Breaker/PTs/Relays, work order unassigned
20 Estimated Total Cost \$50,000. Initial engineering estimate to be further refined
21 when WO is written.

22 Pierce Mills Switches, work order unassigned
23 Estimated Total Cost \$5,000. Initial engineering estimate to be further refined
24 when WO is written.

25 Gage Structure Repair, work order unassigned
26

1 Estimated Total Cost \$15,000. Initial engineering estimate to be further refined
2 when WO is written.

3 All projects listed under the rate year are initial engineering budget estimates and
4 will be further refined when the work order is written

5
6 Q. DOES THAT MEET THE STANDARD OF BEING QUANTIFIABLE WITH A
7 REASONABLY HIGH DEGREE OF ACCURACY?

8 A. No. In Docket No. 5983, the Board discussed the issue of requested rate base
9 additions. In the Board's discussion they stated that, "For major items, a cost-benefit
10 analysis should be conducted prior to the rate request, and for smaller items, a financial
11 analysis should be available in support." Clearly, no cost-benefit analysis or financial
12 analysis has been provided. The projects do not meet the known and measurable standard.

13 Based on Mr. Scarzello's rebuttal testimony, the probability of plant going in
14 service as projected is even more of a concern now. As noted on Schedule 21, 10 of the
15 12 rate year projects we took exception with have significant changes. The Company has
16 conceded that two should be removed, seven have a scheduled completion of June 2002
17 and one has been rewritten, reassessed and postponed (Company says it should still be
18 allowed). Any slippage on the June 7, 2002 projects puts them out of the rate year. Even
19 the interim projects have had slippage of three to six months.

20 Q. WHAT ARE THE NEW ADDITIONS TO PRODUCTION PLANT?

21 A. The Company has come up with a list of five new high priority safety projects.
22 These projects are replacements for delayed or canceled projects. The updating of the
23 original filing with filler projects is not appropriate. The new additions requested, as part
24 of rebuttal, should not be and have not been allowed in the past by the Board.

25 Q. WHAT ADJUSTMENT IS NOW REQUIRED?

1 A. The Company's original filing for production plant should be reduced by
2 \$532,916.

3 Transmission

4 Q. HAVE YOU REVIEWED MR. BUDRO'S REBUTTAL TESTIMONY?

5 A. Yes. He has suggested that we are not qualified to determine whether the
6 construction estimates are within a reasonable degree of accuracy and he states that,
7 "There is no specific factual evidence to suggest that those projects won't be completed as
8 planned." Mr. Budro also suggests that we implied that the transmission additions
9 included growth.

10 Q. DO YOU FEEL YOU ARE QUALIFIED TO EVALUATE WHETHER COSTS ARE
11 SUPPORTED?

12 A. Yes. As accountants we have accumulated years of audit experience and analysis
13 of rate filings. In addition, we have recommended, to the Board, that projects do not meet
14 the known and measurable standard and the Board has accepted our recommendations.
15 As experienced accountants and regulatory analysts, we are well qualified in determining
16 what constitutes support for an amount. The Department's data request 9-3 asked for
17 "support for the estimated cost" of each project. The response breaks \$200,000 into four
18 lines with a broad description for each line. This is not support. A close review of pages
19 52 and 53 of Exhibit DPS-L&A-4 will reveal that support for the transmission substation
20 rate year projects has not been sufficiently provided.

21 As was stated earlier, the Board, in Docket No. 5983, found that a cost benefit
22 analysis or financial analysis should be conducted prior to the rate request and be available
23 as support. DPS 9-3 does not meet that criteria.

1 Q. IS THERE ANY FACTUAL EVIDENCE TO SUGGEST PROJECTS WILL NOT BE
2 COMPLETED AS ORIGINALLY PLANNED?

3 A. Yes. We indicated in our original prefiled testimony that this was a problem and
4 we provided an example. This delay is not an uncommon occurrence. For example, an
5 examination of the work orders for the test year transmission substations revealed seven of
6 the eight projects listed were completed later than projected. The eighth project,
7 Workstation Control Center, WO 6057, did not have a projected completion date on the
8 work order. That project, however, was initiated in January 1999 and was in service in
9 February 2000. A review of the interim year projects with work orders revealed only one
10 of seven projects was completed as scheduled or is expected to be completed. That one
11 project is expected to be completed in June 2001. Similar findings were noted with the
12 transmission line projects.

13 Q. DID YOU SUGGEST THAT GROWTH WAS INCLUDED IN THE TRANSMISSION
14 PROJECTS IN THE ORIGINAL FILING?

15 A. No. The question and answer Mr. Budro referenced was a general observation
16 about "other projects" occurring in lieu of the projects requested in the filing. For
17 example, a typical argument we hear is, "if we do not do the identified project we will do a
18 different one." The problem with that argument is, as we stated on page 37, line 17 of our
19 original testimony, we do not know the cost, whether it is growth related or if cost savings
20 will occur.

21 Q. DID THE COMPANY ACCEPT ANY OF YOUR RECOMMENDATIONS?

22 A. Yes. The Company agreed with our adjustment to three blanket Work Order 32
23 changes and our increase in cost to Work Order 6172. Mr. Budro indicates that two
24 projects, the GPS Time Sync and the Battery Replacement, are included in one of the

1 blank work orders, but he does not indicate that separate project costs should be removed
2 or if the copy has removed them.

3 Q. HAVE YOU CHANGED YOUR POSITION BASED ON THE COMPANY
4 REBUTTAL TESTIMONY?

5 A. Yes. Mr. Budro indicated the switches for the Taftsville Substation have been
6 ordered. Even if slippage occurs, it is probable this project will be completed before the
7 end of the rate year. We will, subject to the Company providing a copy of Work Order
8 6324 for the SCADA Upgrade with supporting detail for the cost, accept the adjusted
9 project cost of \$266,380.

10 Q. THE COMPANY'S CLAIM THAT THE PROJECTS ARE MEASURABLE WITH A
11 REASONABLE DEGREE OF ACCURACY AND HAVE A HIGH PROBABILITY OF
12 BEING IN EFFECT IN THE RATE YEAR. DO YOU AGREE?

13 A. No. First, the claim that projects are "highly likely to be in place in the rate year"
14 is not supported as we stated earlier. The fact is that slippage is common, and even Mr.
15 Budro identified a deferral on the East Fairfax Breaker. This project was to be completed
16 in October 2001, now the projected completion date is May 2002, which leaves little room
17 in the rate year for additional slippage for a project that has not started.

18 The change in the cost of the SCADA Upgrade is evidence that the estimates are
19 not fully supported. The cost changed 15.8% by the time a work order was assigned.
20 History also provides evidence that the estimates for the work orders are not always on
21 target. Listed below are three projects with their original work order cost projection, the
22 amount reflected in the filing and the actual cost:

	<u>Project</u>	<u>Work Order Cost</u>	<u>Filing Cost</u>	<u>Actual Cost</u>
1				
2	Install Relays, WO 6083	115,940	99,322	99,322
3	Switchgear Post Rd., WO 9961	272,000	226,020	219,780
4	Rec. Middlebury, WO 9939	63,320	52,600	52,660

5 The support for the estimated project costs, requested by the Company, has not
6 been provided.

7 Q. IS MR. BUDRO'S CLAIM THAT YOU HAVE NOT PRESENTED EVIDENCE TO
8 SUPPORT YOUR VIEWPOINT ACCURATE?

9 A. No. We identified that the cost support provided, by the Company, for the
10 projects in question are no more than numbers with a broad description. (See DPS-L&A-
11 4, pages 52 and 53.) We also identified the historical slippage problem. We have
12 supported our position. The Company's rebuttal testimony was repetitive statements that
13 the projects are measurable and will be in place in the rate year. The burden of proof was
14 on the Company and they have not supplied the requested support. By including the
15 Taftsville Substation and the SCADA Upgrade, the transmission plant additions allowed
16 should be \$2,520,744. This is \$636,000 less than the Company's original request of
17 \$3,157,000.

18 Distribution Plant

19 Q. PLEASE EXPLAIN WHY YOU HAVE EXCLUDED THE THREE RATE YEAR
20 DISTRIBUTION SUBSTATION PROJECTS?

21 A. The support provided for the Substation Clearance Improvements, Installation of
22 Bypass Switches and the Wallingford S/S HS fuse configuration is minimal. The original
23 prefiled testimony of Mr. Budro consists of a very general description of the projects. The

1 response to DPS 3-93 indicates a three-month slip for the Wallingford project. In addition
2 to Mr. Budro's rebuttal testimony, which states the "Projects are highly likely to be in
3 place in the rate year and that their cost is estimated with a high degree of accuracy."
4 There is no work order, no cost benefit analysis, no cost analysis and simply put, no
5 support. The burden of proof, to supply us with cost support and evidence that the
6 project will be completed before the end of the rate year, lies with the Company. That
7 burden has not been met and, therefore, the costs should not be allowed.

8 Q. HAS THE REBUTTAL TESTIMONY OF MR. WHITE CAUSED YOU TO CHANGE
9 YOUR ORIGINAL RECOMMENDATIONS ON DISTRIBUTION PURCHASES AND
10 RECONSTRUCTION?

11 A. Yes. As indicated in our prefiled testimony, an adjustment was made to
12 Regulators and Capacitors, WO 37, due to the higher than average projected costs in the
13 rate year. Mr. White, in rebuttal, provides an explanation for why the expenditures are
14 projected to be higher. He also provided a significant amount of additional justification in
15 his exhibits. One exhibit indicates that it includes guesswork in most cases for added costs
16 for distribution work over two years. With the additional information, we will accept the
17 Company's revised projected 13-month average of \$364,121 for Regulators and
18 Capacitors, WO 37.

19 The second change pertains to Meters, WO 38. The unusual write off of meter
20 inventory in 1997 does not warrant consideration. However, we will note that the
21 Company has selected to exclude the unusual year from the average, in this scenario, but
22 in the area of overtime payroll, the Company has not only not considered doing a
23 comparable analogy they have elected to keep the unusual level of costs for the rate year
24 overtime. We are also accepting the other proposed changes to costs as described in
25 testimony and exhibits, with three qualifications. First, the Company must identify any

1 retirements and adjust for them. Second, the testimony and exhibits suggest that potential
2 cost savings could result from the meter changeover (i.e., reduction in meter failures,
3 managing load requirements) and an estimate of the savings needs to be provided. Finally,
4 a reconciliation between the original plant schedule and Exhibit White 8 is necessary to
5 verify that each change discussed has been made.

6 Q. ARE YOU ADJUSTING THE DISTRIBUTION RECONSTRUCTION COSTS?

7 A. We are awaiting responses to gain a better understanding of Mr. White's
8 explanation of the backlog. At present, we are not convinced because if the plant is in
9 service it does not seem logical that it will take ten months to record it into Plant in
10 Service. Second, information provided in response to DPS 3-99 indicates the amounts in
11 the filing are budgeted and proposed spending, not the backlog referred to by Mr. White.
12 No changes are supported at this time. After making the adjustments to WO 37 and WO
13 38, as described above, the appropriate 13-month average for distribution plant additions
14 is \$10,013,833. This is \$2,209,000 less than the Company's original request of
15 \$12,223,000.

16 Facilities

17 Q. ARE THERE REVISIONS TO YOUR RECOMMENDED DISALLOWANCE OF
18 FACILITY ADDITIONS?

19 A. Yes. A combination of information supplied previously, the rebuttal testimony of
20 Ms. Mandolare, Work Order 6334, capital budget information for 2001 and some
21 consideration given to the historical spending identified in Exhibit Frankiewicz 6. On
22 Exhibit DPS-L&A-5, page 5 of 6, we have identified any revisions to our original
23 recommendation with the letter "R".

1 Q. WHAT ABOUT THE CHANGE THE COMPANY MADE TO THE RUTLAND AREA
2 CENTRAL SCHEDULING PROJECT?

3 A. The only additional information received on the Rutland Area Central Scheduling
4 project was the ten lines of rebuttal testimony by Ms. Mandolare. There was no
5 supporting detail or cost benefit analysis provided that would substantiate the improved
6 “operational efficiencies.”

7 Q. WHAT IS YOUR RECOMMENDATION FOR FACILITIES ADDITIONS?

8 A. Our revised recommendation is an addition of \$892,929 to facilities. This is
9 \$48,000 less than the Company’s original request of \$941,000.

10 Information Systems

11 Q. ARE YOU REFLECTING ANY CHANGES TO YOUR INFORMATION SYSTEMS
12 RECOMMENDATIONS?

13 A. Yes. The Company originally provided explanations as to how the rate year
14 additions were determined. The historical spending has consistently exceeded the
15 projected level of spending in the rate year; the only uncertainty was whether the projects
16 would be in service during the rate year. Rebuttal testimony by Mr. Monder has indicated
17 that work orders have been issued for the Server Upgrade, the Disaster Recovery
18 Enhancements and the PC Equipment. The work order for the District Server
19 Environment project is in the development process. A copy of the work order has been
20 requested.

21 A review of work orders previously received indicated that projected completion
22 dates range from three months to one year from issuance. Actual completion for those
23 work orders was four months to three years after the projected completion date. One
24 exception was Work Order 6158, which appears to be completed as projected. Most of

1 the slippage is at least one year. Based on the projected in service dates of August 2001
2 and December 2001, there is good probability (based on historical evidence) that the
3 projects will not be completed until after the rate year. However, since costs will be
4 incurred and because of the type of purchases that will be made, it is possible that some of
5 the equipment will be in service by the end of the rate year. Based on that presumption,
6 we are recommending that ½ of the project costs for the Server Environment Upgrade,
7 the Disaster Recovery Enhancements and the PC Equipment be allowed. This would
8 increase the 13-month average plant balance of \$69,235 to \$3,931,515 before adjusting
9 for the affect of plant retirements on Work Orders 6061 and 6158. This information needs
10 to be provided by the Company.

11 Q. HOW DOES YOUR TENTATIVE RECOMMENDATION COMPARE TO THE
12 COMPANY REQUEST?

13 A. The \$3,931,515 is \$20,000 higher than the Company's original request of
14 \$3,912,000.

15 Communications

16 Q. ARE THERE ANY CHANGES TO YOUR COMMUNICATIONS PLANT
17 RECOMMENDATIONS?

18 A. Yes. We are now recommending that the Fiber Loop Completion (WO 6246), the
19 test equipment and microwave additions be allowed in plant additions.

1 Q. IS THE COMMUNICATIONS (SIC-INFORMATION SYSTEMS) DEPARTMENT
2 CONSISTENTLY HITTING THE MARK IN TERMS OF TIMING AND COST ON
3 BUDGETED PRODUCTS AS MR. MONDER CLAIMS?

4 A. No. They have hit the mark on some projects, but others have had delays. A
5 problem in verifying this claim is that the Company did not always enter a projected
6 completion date on the work order. The following is a list of eight projects and their
7 results:

<u>Project</u>	<u>Initiated</u>	<u>Projected</u>	<u>Filing</u>	<u>Actual</u>
Purchase Voiceover WO 6005	12/98	N/A	12/99	09/00
Radio Network WO 9631	06/96	N/A	12/99	12/99
Install Radio/Ant. WO 6120	08/99	12/99	04/00	04/00
Install Microwave WO 6085	04/99	12/99	05/00	12/00
Install Back-Up WO 9873	12/97	05/98	10/99	10/99
Radio Consoles WO 6106	07/99	09/99	09/00	12/00
Rep. Mobile Radios WO 6178	03/00	12/00	10/00	N/A
CVPS Backbone WO 6180	03/00	07/00	09/00	12/00

17 * N/A - Not Available

18 As can be seen, delays of two months to 17 months have occurred between the
19 projected and actual completion dates. This delay is added to the approximate two to
20 eight months time lag between the initiation of the work order and the projected
21 completion date. On the assumption that the original projected completion date is
22 approximately four months and the completion delay is five months, you are looking at an
23 estimated minimum nine month completion period. The key, now, in determining the
24 completion date of the proposed rate year projects is the actual start date.

25 The PBX is still an uncertainty as to the in service date. The project is scheduled
26 to last eight months and is a large project so the delays discussed earlier are considered to
27 be conservative for this project. In addition, the Company rebuttal testimony dated March
28 30, 2001, provided no indication that the April 1, 2001 start date was on target. Finally,

1 the quote expired in September 2000. The size and time of this project makes it an
2 uncertainty.

3 Q. WHAT IS YOUR RECOMMENDATION FOR COMMUNICATION PLANTS?

4 A. Communication plant additions of \$1,254,638 should be allowed. This is
5 \$333,000 less than the Company's originally filed request of \$1,588,000.

6 Plant Addition Summary

7 Q. PLEASE SUMMARIZE YOUR FINDINGS ON PLANT ADDITIONS.

8 A. As shown on our revised Schedule 13, the Company's original requested plant
9 additions should be reduced \$3,740,000. The adjustment removes a reasonable level of
10 costs that are not known and measurable. The want, or in some cases, the need for a
11 project is not in and of itself sufficient to make a project known and measurable. Cost
12 estimates need to be supported by a project cost analysis and/or cost benefit analysis. A
13 number of descriptions are not sufficient.

14 The probability of occurrence has to be based on more than good intentions. The
15 history of slippage and the fact that projects have not been initiated are prime
16 determinants. A wish list does not meet the known and measurable standard.

17 Working Capital

18 Q. DID YOU REVIEW THE JOHN J. HOLTMAN AND JOHN K. LAFASO'S JOINT
19 REBUTTAL TESTIMONY ON WORKING CAPITAL?

20 A. Yes.

1 Q. DID THE COMPANY'S REBUTTAL TESTIMONY ON WORKING CAPITAL
2 AFFECT YOUR ORIGINAL RECOMMENDATION?

3 A. No. The Company now attempts to justify its position that working capital would
4 be greater by identifying a change in billing by Vermont Yankee and changes in tax deposit
5 requirements. The change to Vermont Yankee occurred in May 2000, and the tax deposit
6 change occurred in 1993, which suggests that the Company did little to evaluate any
7 changes in the working capital requirement, let alone do any analysis to support the
8 Company's position. No mention of the changes were identified in responses to the
9 Department.

10 Q. IS THE COMPANY REBUTTAL TESTIMONY CORRECT REGARDING THE
11 WEIGHTING OF THE CHECK CLEARING LAG?

12 A. Yes. Weighting would provide a more accurate lag calculation. Our calculation
13 was made on a simple basis to substantiate our position that a lag occurs. The calculation
14 lag of 4.58 days was not used for purchase power because the lag applied primarily to the
15 lower purchase power costs.

16 Q. IS THE COMPANY'S CLAIM CORRECT THAT ADDING THE LAG "IS NEITHER
17 APPROPRIATE NOR SUPPORTABLE?"

18 A. No. In fact, the clearing lag we used is conservative. The clearing lag was
19 calculated using purchase power invoices because that was the best available information
20 to use under the circumstances. The calculation served as a basis for determining a
21 clearing lag. Our calculation reflects that and the Company witnesses, Holtman and
22 Lafaso, stated that they "Agree theoretically with using a check clearing lag." The
23 Company calculation shows that a weighted lag of one day does exist for purchase power.
24 We proposed the clearing lag only for the other O&M expense calculation of the lag. The

1 other O&M expense is different because it does not utilize wire transfers in the same
2 proportion as the purchase power payments are made. We have modified the Company's
3 calculation to include only payments by checks. The calculated weighted check clearing
4 lag is seven days (WP-WC5). This is sufficient evidence that a clearing lag exists and that
5 the three day lag added to O&M Expense Other is conservative. Our recommended net
6 O&M Operating Expense Lag of 9.35 days is reasonable.

7 Q. DID THE COMPANY PROVIDE ANY EVIDENCE THAT A DETAILED ANALYSIS
8 WAS PERFORMED TO SUBSTANTIATE THAT THE CUSTOMER PAYMENT LAG
9 HAS LENGTHENED?

10 A. No. The Company falls back on the response to DPS 7-19. The response shows a
11 quick comparison of a portion of accounts receivable. While it does give the impression
12 that a significant change has occurred, it is only a piece of the information that must be
13 considered. Some of the increase can be attributed to the fact that revenue, in 2000, was
14 about 20% higher. Accounts receivable is less than 10% of the total accounts receivable
15 outstanding. The Company's claimed justification is only a piece of the so called "back of
16 the napkin" approach we utilized.

17 Q. IS THE COMPANY'S CHARACTERIZATION OF YOUR REVENUE LAG
18 CALCULATION AS "BACK OF THE NAPKIN" APPROPRIATE?

19 A. No. We requested, in DPS 7-20, the detail required to calculate the collection as
20 described in the Holtman/Lafaso rebuttal testimony, but the Company said the information
21 was not available. The Department should not be penalized for using the best available
22 alternative to calculating a revenue lag when the Company is unable to retrieve historical
23 information from the Company's accounting records. The burden of proof is on the
24 Company, we provided the best available evidence of what collection lag currently exists

1 and the Company has not provided any evidence to rebut that calculation. Therefore, the
2 recommended reduction of 6.49 days to the collection lag should be made.

3 Q. DO YOU HAVE ANY COMMENTS ON THE COMPANY REBUTTAL TESTIMONY
4 TO YOUR CONCERNS ON THE RECONCILIATION OF ACCOUNTS
5 RECEIVABLE AND THE COMPANY'S COLLECTION POLICY?

6 A. Yes. The Company refers to DPS 7-1 and references an internal audit for which
7 "no report was issued." This internal audit was not the one relied on. The report relied
8 on was a cash processing audit. The observation by Arthur Anderson states, "The Cash
9 Processing Department is not following the policy of sending the delinquent account
10 notification letters to inactive customers..." The Company even references this report
11 later in the rebuttal testimony as a problem with collections. The identified problem exists.

12 Q. WHAT ADJUSTMENTS SHOULD BE MADE TO THE WORKING CAPITAL
13 CALCULATION?

14 A. As discussed in our March 9, 2001, prefiled testimony, we are reducing the
15 revenue lag by four days and increasing the expense lead by three days for check clearing.
16 We did not adjust for a longer calculated revenue lag, the noncash expenses in the other
17 O&M lead calculation or the approximate four additional days for checks to clear. The
18 conservative adjustments and the impact from other operating and rate base adjustments
19 made by the Department, reduces the Company's requested working capital requirement
20 by \$3.024 million. This adjustment, along with the supporting calculations, is provided on
21 our Revised Schedule 15.

22 **IV. ACCOUNTING IMPLICATIONS OF DEPARTMENT RECOMMENDATIONS**

1 Q. IN HIS REBUTTAL TESTIMONY, WITNESS BENJAMIN A. MCKNIGHT
2 CONTENTS THAT THE DEPARTMENT'S PRIMARY RECOMMENDATION WITH
3 REGARDS TO HYDRO QUEBEC WOULD REQUIRE CVPS TO DISCONTINUE
4 USE OF SFAS NO. 71 FOR FINANCIAL ACCOUNTING PURPOSES. DO YOU
5 AGREE WITH HIS CONCLUSION?

6 A. Definitely not. If Department Witness William Steinhurst's primary
7 recommendation with regards to Hydro Quebec contract issues is adopted by the Board,
8 CVPS would not be required to discontinue use of Statement of Financial Accounting
9 Standard (SFAS) No. 71 for financial reporting purposes. As indicated in Mr. Steinhurst's
10 prefiled testimony, dated March 9, 2001, the Department's primary recommendation is
11 that the disallowances and penalties imposed be equivalent to a one-time write down of no
12 more than \$25 million. Along with this disallowance or penalty, Mr. Steinhurst
13 recommended that the Board also make clear that the ordered disallowances or penalties
14 provide finality as to prudence of the Contract and its management to date, specifically
15 stating that the contract will then be treated as if it were used and useful. He also
16 recommended that the wording of the Order clearly indicate that the disallowance or
17 penalty will be a one-time write down to bring closure to this issue.

18 Q. WHAT IS SFAS NO. 71?

19 A. SFAS No. 71, *Accounting for the Effects of Certain Types of Regulation*, provides
20 guidance to regulated public utilities in preparing their financial statements. It takes into
21 consideration situations that are unique to regulated public utilities. It is under SFAS No.
22 71 that qualifying utilities are permitted to capitalize costs as regulatory assets and
23 recognize obligations as regulatory liabilities for financial accounting purposes. In order
24 to recognize a regulatory asset, it must be probable that the regulatory agency will permit
25 the capitalized cost to be included in a future revenue requirement calculation. In other

1 words, it must be likely that the regulatory agency will permit the inclusion of the costs,
2 through a method such as amortization, in the revenue requirement calculations for
3 effective inclusion of such costs in rates. As stated within the Summary section of SFAS
4 No. 71:

5 For a number of reasons, revenues intended to cover some costs are provided
6 either before or after the costs are incurred. If regulation provides assurance that
7 incurred costs will be recovered in the future, this Statement requires companies to
8 capitalize those costs. If current recovery is provided for costs that are expected
9 to be incurred in the future, this Statement requires companies to recognize those
10 current receipts as liabilities.

11 The entire text of SFAS No. 71 was provided as Exhibit CVPS-BAM-3, attached
12 to Mr. McKnight's rebuttal testimony. It is SFAS No. 71 that allows regulated utilities to
13 set up regulatory assets for costs, which are allowable for recovery in a period other than
14 the period the cost would normally be charged to expense.

15 Q. WHAT WOULD BE THE IMPACT OF THE DISCONTINUANCE OF SFAS NO. 71
16 FOR FINANCIAL ACCOUNTING PURPOSES?

17 A. Essentially, CVPS would be required to write-off all of the regulatory assets
18 contained on its books. It would no longer be permitted to follow the special accounting
19 treatment allowed for qualifying public utilities and would instead be required to record
20 costs as expenses in the period incurred. It would no longer be able to capitalize costs as
21 regulatory assets.

22 Q. ON WHAT BASIS DOES MR. KNIGHT CONTEND THAT THE DEPARTMENT'S

1 PRIMARY RECOMMENDATION WOULD REQUIRE THE DISCONTINUANCE OF
2 SFAS NO. 71?

3 A. Mr. McKnight states that he “believes” there are two “significant trigger points”
4 which indicate that an enterprise no longer meets the criteria of SFAS No. 71. These two
5 trigger points, as discussed in his rebuttal testimony at page 16, are:

- 6 1. If the current form of rate regulation results in an extended rate
7 moratorium or a regulatory process which precludes the enterprise for an
8 extended period (in excess of five years) from adjusting rates to reflect its
9 cost of providing services; and
- 10 2. If the regulatory process results or is expected to result in the enterprise
11 earning significantly less (250-300 basis points) than its allowed or a
12 reasonable current rate of return for an extended period of (three or four
13 years).

14 The witness contends that both of these “trigger points” would occur if the
15 Company is not likely to earn its allowed rate of return in the period rates from this
16 proceeding are to be in effect. It is Mr. McKnight’s opinion that the rate treatment,
17 recommended by the Department, would not “afford Central Vermont any reasonable
18 opportunity to earn its allowed return on an annualized basis once the new rates
19 established in this proceeding would go into effect.” He continues his discussion, stating
20 “When one recognizes that Central Vermont has not earned or been afforded the
21 opportunity to earn its allowed ROE over the past three years, I could not conclude that
22 Central Vermont was subject to a form of ratemaking that provides it an opportunity to
23 recover its costs and earn a return as would be necessary to remain on SFAS No. 71.”
24 (McKnight Rebuttal, page 6)

25 Q. ARE THE TWO TRIGGER POINTS IDENTIFIED BY MR. MCKNIGHT

1 CONTAINED IN THE EXPLICIT LANGUAGE OF SFAS NO. 71?

2 A. No. As previously mentioned, a full copy of SFAS No. 71 was included as an
3 exhibit attached to Mr. McKnight's testimony. It is very important to recognize that the
4 Department's recommendation in this case would allow the Company an opportunity to
5 earn a fair and reasonable rate of return on allowable costs. The Department is
6 recommending that the Hydro Quebec \$25 million write-down be made as a disallowance
7 or penalty pertaining to that issue and that it bring final resolution to the Hydro Quebec
8 contract issue for ratemaking purposes. Thus, it would not be considered an allowable
9 cost for determining the overall earned rate of return. All of the Department's remaining
10 adjustments, along with the Hydro Quebec one-time write-down, result in the utility being
11 afforded the opportunity to earn a fair and reasonable rate of return based on prudent and
12 allowable costs and investments. The term "allowable" is specifically used frequently
13 throughout SFAS No. 71. SFAS No. 71 does not require that a regulatory commission
14 authorize recovery of each and every cost incurred by a utility in order for the utility to be
15 able to use SFAS No. 71 for accounting purposes. For example, regulatory commissions
16 consistently require that certain costs incurred by utilities, such as contributions, donations
17 and lobbying costs, be recorded below the line and excluded from the calculation of
18 revenue requirement. SFAS No. 71 does not require that regulatory commissions include
19 each and every cost, including imprudent costs, in the revenue requirement calculation for
20 recovery from ratepayers.

21 Q. COULD YOU PLEASE EXPAND ON HOW THE TERM "ALLOWABLE" IS USED

1 IN SFAS NO. 71 AND OTHER REGULATORY PRONOUNCEMENTS?

2 A. Yes. The second sentence in paragraph 1 in the Introduction section of SFAS No.
3 71 states that "Regulators use a variety of mechanisms to estimate a regulated enterprise's
4 allowable costs, and they allow the enterprise to charge rates that are intended to produce
5 revenue approximately equal to those allowable costs." The pronouncement continues,
6 stating that "Specific costs that are allowable for rate-making purposes result in revenue
7 approximately equal to those costs." SFAS No. 71 defines allowable as all costs for which
8 revenue is intended to provide recovery.

9 The criteria that must be met for the application of SFAS No. 71 are provided in
10 paragraph 5 of the statement, under subpoints (a) through (c). The first criterion is that
11 the rates for regulated services are established under the approval of an independent, third-
12 party regulator. The second criterion is that the regulated rates are "...designed to recover
13 the specific enterprise's cost of providing the regulated services or products." The third
14 criterion deals with anticipated changes in the levels of demand or competition and the
15 impact of such on the recovery of costs rates are established to recover. It is apparently
16 under the second criteria that Mr. McKnight has determined his "trigger points" identified
17 in his testimony. However, the criteria contained in paragraph 5 deals with "allowable"
18 costs, not all incurred costs.

19 Q. PLEASE EXPLAIN.

20 A. First, as background, we would like to discuss SFAS No. 101, *Regulated*
21 *Enterprises -- Accounting for the Discontinuation of Application of FASB Statement No.*
22 *71*, which was provided with Mr. McKnight's testimony as CVPS Exhibit-BAM-6.
23 Paragraph 4 of that statement indicates that failure of a utility to continue to meet the
24 criteria in paragraph 5 of SFAS No. 71 can result from different causes. The paragraph
25 provides four examples, consisting of: (1) deregulation; (2) change in regulator's

1 approach, shifting from cost-based ratemaking to another regulation form; (3) increased
2 competition limiting the ability to sell services at rates that will recover costs; and (4)
3 regulatory actions resulting from resistance to increases in rates that limit utility's ability to
4 sell services at rates that will recover costs if the utility can not obtain relief from prior
5 regulatory actions through appeals. SFAS No. 101, Appendix B: Basis for Conclusions,
6 Overall Conclusion on the Discontinuance of Application of Statement 71, paragraph 36,
7 states that the term "costs" used in paragraph 4 of the statement (discussed above
8 regarding examples of reasons to discontinue SFAS No. 71) is consistent with the usage
9 of the term "costs" in paragraph 5 of SFAS No. 71. The last sentence of paragraph 36
10 states, "As explained in paragraph 67 of the Basis for Conclusions to Statement 71, the
11 term costs in paragraph 5 of Statement 71 is based on allowable costs."

12 Q. WHAT DOES PARAGRAPH 67 OF THE BASIS FOR CONCLUSIONS TO
13 STATEMENT 71 STATE?

14 A. The paragraph, which is included in Exhibit-CVPS-BAM-3, at page 22, states:
15 The Board does not intend the last criterion as a requirement that the enterprise
16 earn a fair return on shareholders' investment under all conditions; an enterprise
17 can earn less than a fair return for many reasons unrelated to the ability to bill and
18 collect rates that will recover allowable costs...

19 The phrase "allowable costs" is footnoted in the paragraph, indicating that "...the term
20 allowable costs is used here to include earnings permitted on shareholders' investment."

21 Q. IF THE BOARD ADOPTS THE DEPARTMENT'S RECOMMENDATIONS, WOULD

1 CVPS'S RATES STILL BE COST BASED?

2 A. Yes. CVPS's rates would still be calculated based on allowable costs; thus,
3 CVPS's rates would still be cost-based. The term "cost based rates" does not mean that
4 any and all costs are automatically included in the rate calculation. Disallowance of
5 certain costs for appropriateness, penalties or prudence does not result in rates that are not
6 cost based. CVPS's rates would still be based on allowable costs. There would still be
7 the cause-and-effect relationship between CVPS's allowable costs and the determined
8 rates.

9 The Department's recommendations, if adopted, would still result in the
10 Company's rates being determined based on "allowable" costs. It would allow CVPS the
11 opportunity to earn a fair rate of return calculated based on allowable costs and
12 investment, excluding the \$25 million disallowance associated with Hydro Quebec.

13 Q. YOU PREVIOUSLY DISCUSSED SFAS NO. 101, *REGULATED ENTERPRISES –*
14 *ACCOUNTING FOR THE DISCONTINUATION OF APPLICATION OF FASB*
15 *STATEMENT NO. 71*. DOES SFAS NO. 101 PROVIDE DETAILED GUIDELINES
16 FOR DETERMINING WHETHER OR NOT THE APPLICATION OF SFAS NO. 71
17 SHOULD BE DISCONTINUED?

18 A. No. Previously, we mentioned some examples found in SFAS No. 101 of factors
19 that can cause utilities to no longer meet the necessary criteria contained in paragraph 5 of
20 SFAS No. 71. However, the Financial Accounting Standards Board intentionally did not
21 provide detailed guidance for determining whether or not SFAS No. 71 should be
22 discontinued. Paragraph 35 of SFAS No. 101 (which can be found in Exhibit-CVPS-
23 BAM-6 at page 11) specifically states as follows:

24 This Statement does not provide detailed guidance for reaching judgements about

1 whether application of Statement 71 should be discontinued. Similarly, Statement
2 71 does not provide detailed guidance for reaching judgments about whether it is
3 appropriate to apply Statement 71. Because applicability of Statement 71 is and
4 must remain a matter of judgment and because the objectives are clear, the Board
5 decided that it was unnecessary to prescribe detailed guidance for reaching the
6 judgments required by this Statement and by Statement 71.

7 The determination of whether or not CVPS would be required to discontinue use
8 of SFAS No 71 if the Department's primary recommendations are adopted by the Board is
9 not as cut and dry as CVPS rebuttal witnesses Boyle and McKnight would lead one to
10 believe.

11 Mr. McKnight's testimony focuses on all costs incurred by CVPS, not on costs
12 determined to be "allowable" by the regulatory commission. SFAS No. 71 clearly
13 addresses allowable costs, not all incurred costs in establishing the criteria for application
14 of SFAS No. 71. It is our opinion that the CVPS would not be required to discontinue
15 use of SFAS No. 71 for financial accounting purposes if the Department's primary
16 recommendations are adopted.

17 Q. DOES THIS COMPLETE YOUR SURREBUTTAL TESTIMONY?

18 A. Yes, it does.